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Code of Ethics: A Conceptual Model and Preliminary Results

Pierre Pawliw

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Abstract

Academic research into codes of ethics has given us valuable information on the subject but has failed to provide an all-encompassing understanding of the contents of actual codes. This paper looks at what is presently known about this subject, presents a conceptual model that integrates the different elements that go into a code of ethics, describes the dynamics that explains why each company's code of ethics has a distinct content, and presents preliminary results obtained after having analyzed a cross-section of the code of ethics of member companies of the Ethics and Compliance Officer Association.

About the author

Pierre Pawliw is a DBA student at the Université de Sherbrooke, in Sherbrooke, Québec, Canada.

Sprott Research Program
research@sprott.carleton.ca
Sprott School of Business • Carleton University • 1125 Colonel By Drive • Ottawa • Canada • K1S 5B6

Carleton University
Sprott
School of Business

710 Dunton Tower
1125 Colonel By Drive
Ottawa, ON K1S 5B6 Canada
Tel: (613) 520-2388
Fax: (613) 520-4427
www.business.carleton.ca

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Pierre Pawliw
Université de Sherbrooke

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Introduction

There are many studies on the topic of codes of ethics. Every one of them provides us with a better understanding of what they are, what they try to accomplish and what they contain. Notwithstanding prescriptive accounts of what codes of ethics should contain, few have succeeded in fitting all the pieces together to give us a general understanding of the various elements that shape the contents of codes of ethics found in today's companies. We consider that the lack of a conceptual model constitutes a problem for researchers and business people alike. It hinders research for anyone working in the field of business ethics that requires a general understanding of this topic in order to pursue an inquiry into related subjects. And it makes it more difficult for business people to grasp the many facets that they should consider when writing a code of ethics for their own organization.

This text has four main sections. First, it presents a synthesis of the research done on the topic in order to derive a conceptual model of codes of ethics. Second, it presents the conceptual model that identifies the main elements one is susceptible to find in a code of ethics, and it describes the dynamics between these elements responsible for shaping a code's content. Third, using the conceptual model, it presents the results of a content analysis of a number of codes of ethics. The analysis was carried out in order to verify whether the conceptual model correctly describes actual codes of ethics. Fourth, it discusses the implications of these results for the conceptual model and for further research.

Definition

The literature on codes of ethics does not offer one truly comprehensive definition. Therefore in order to grasp its full meaning, we must make up a composite definition that integrates the many components found in a code of ethics. Taken from a business or managerial perspective, Stevens (1990) tells us that it is a written document, of any length and form, intended to impact employee behaviour. From that point of view, it is a managerial tool used to shape change. Boudreaux and Steiner (2005) consider that the document forms the underpinning of a comprehensive program whose objective is to ensure ethical behaviour and decision-making in the organization. And Kaptein (2004) informs us that the document is company specific.

Taken from a content perspective, Wood and Rimmer (2003) tell us that a code of ethics contains an organization's statement of norms and beliefs, and fundamental principles that provide guidance in cases where no specific rule exists. Sanderson and Varner (1984) say that the document outlines the company's philosophy and rules of acceptable behaviour. And Schwartz (2002) considers that it contains moral standards.

Finally, from the perspective of what it is supposed to do, Langlois and Schlegelmilch (1990) tell us that its contents serve to lay down the company's responsibility to various stakeholders: employees, shareholders, the environment and any other aspect external to the company.

When we gather all these elements together, we come up with this composite definition: a code of ethics is a management tool in the form of a written document in which the company states the principles, norms and standards on which employee responsibilities are based as well as company responsibilities towards various stakeholders.

History

The history of codes of ethics spans almost over a century, though most developments are quite recent and occurring in the last fifty years. Wood and Rimmer (2003) trace the first code of ethics to 1913 when JC Penney became the first company to have one. And in 1924, Heermance was the first to write a book on the subject, though Stevens (1994) considers that it mostly developed the topic of codes of ethics applicable to the various professions. Later, in the 1950's, Benson (1989) notes that corporations started to introduce 'Creeds' or 'Credos' as a way to set an ethical climate. Then in the late 1950's, the first in a number of scandals occurred that influenced the spread of code of ethics in the corporate world. The US Department of Justice investigated the antitrust conviction of high-ranking officials of electrical manufacturing companies. The Business Ethics Advisory Council was established and it encouraged the adoption and updating of company and industrial codes of ethics. A second set of scandals took place in the 1970's. As Chatov (1980) recalls, the Foreign Corrupt Practices Act was adopted as a response to an investigation of unreported political payments that were discovered in connection with the Watergate incidents. This peace of legislation is credited with the recent growth and popularity of corporate codes of ethics. A third series of scandals came in the mid 1980's. Pelfrey and Peacock (1991) report that the many revelations of dishonest accountants using misleading financial reports brought about the Treadway Commission that recommended that all publicly held companies develop and enforce written codes of corporate conduct. For their part, the 1990's, according to Tulder and Kolk (2000), were marked by a wave of voluntary codes on account that the corporate world was feeling pressure for having supported oppressive regimes, having committed international environmental damage and for outsourcing to countries with inferior labour conditions. Finally, with the new century came the Enron scandal and the SEC's response of the Sarbanes-Oxley Act.

The historical account of the development of codes of ethics seems to suggest that the main drivers of their proliferation have been financial scandals, and the fear of tarnishing brand name and reputation in the public's eye. Also, various government regulatory bodies played an important role in trying to curtail certain corporate behaviours without overly burdening companies. With each new scandal came new guidelines, and companies are now finding themselves in a situation where they adopt a code of ethics basically because they have to.

Business Justification

Considering that a code of ethics is a management tool, what can companies reasonably hope to accomplish with it? Raiborn and Payne (1990) give a partial answer by saying that they can affect the behavior of employees in the organization. Pelfrey and Peacock (1991) furnish a more detailed account. First, they tell us that for the Treadway Commission, the code of ethics is a weapon in the fight against fraudulent financial reporting. Second, they inform us that for the Conference Board it is a way to a) ensure commitment of the CEO to the code; b) help maintain public trust and credibility; c) foster greater managerial professionalism; d) protect against improper employee conduct; e) define ethical behaviour in light of new laws or social standards; f) ensure the maintenance of high ethical standards in the face of changing corporate culture and structure. Berenbeim (2000) gives an additional five reasons: a) enhance reputation and brand image; b) signal the company's commitment to ethical behaviour; c) create a corporate culture and provide a mechanism to operationalize values; d) avoid fines, sanctions and litigation; e) enhance development prospects in emerging economies. On their part, Farrell et al (2002) say that a code of ethics operates as a mechanism to ensure behavioural conformity to standards, and signals the company's competence and integrity to society. Finally, Kaptein (2004) adds that they encourage authorities to relax regulations and controls.

By combining all theses reasons, we develop a mental image that companies have codes of ethics because they contribute to the enhancement of corporate reputation and to the protection of brand image by avoiding fines, sanctions and litigations due to financial fraud and improper employee behaviour by operationalizing values and creating a corporate culture.

Content of Codes of Ethics

Agreeing on the general contents of a code of ethics is not easy. The main problem is that the results obtained by a past study do not corroborate the results of another. What we do find is that one study will list items, or issues, identified in their study sample. Then another study will do the same, but the list provided, though somewhat similar, is not necessarily the same as the list of the first study. How do we explain that? It’s all a question of methodology. Traditionally, codes of ethics have been studied using the same methodology: content analysis. Harris (2001) sums up the method quite well in eight points: a) identify the questions to be asked and the constructs to be used; b) choose the texts to be examined; c) decide on the «unit of analysis»; d) determine the categories into which responses are to be divided; e) generate a code scheme; f) conduct a pilot study and revise the categories and coding scheme; g) collect data; h) assess validity and reliability.

In the case of code of ethics, we have found that what differentiates the various studies in this field are the categories into which they class the different items they find. For example, Chatov (1980) uses two main categories: employee relation to firm, and firm relations to 11 different stakeholders. Cressey and Moore (1983) use three categories: policy areas, authority and compliance procedures. Robin (1989) uses four categories: a) be a dependable organization citizen; b) don't do anything unlawful or improper that will harm the organization; c) be good to our customers; d) other. Farrell et al (2002) examine codes in three areas: a) behaviour and actions discussed in the codes; b) enforcement procedures; c) penalties. Finally, Kaptein (2004) uses five categories: a) stakeholder responsibilities; b) stakeholder principles; c) corporate values; d) internal employee conduct; e) implementation and compliance.

If we were to use the same sample of code of ethics and classify their content according to these different categories we would end up with different accounts of the contents. That's exactly what we have now. In comparing the results of each study, we find they are somewhat similar, but still different. You cannot use one study and conclude that its results give a definitive portrait of the contents of a code of ethics. At best, each study gives a statistical report of the issues that are the most often touched upon in a code of ethics, and then classifies them into general categories used to sum things up and to give a general understanding. They are therefore snapshots, pictures of the contents of the codes of ethics taken at a certain time from a certain angle. What then do we learn from the different snapshots that have been taken? Mostly, we learn a number of general characteristics. We've identified four of them.

First of all, companies do not generally agree on which content should be included in a code of ethics. White and Montgomery (1980) observed that there is a low level of consensus about the ideal content of a code of ethics. They found that there is significant variation in the mix of subjects and their analyses did not permit them to find a pattern of subject selection. However, Sanderson and Varner (1984) were able to discern that 75% of their content was related to complying with federal laws. Even so, Robin et al (1989) found that codes are different from one company to the next and that it is difficult to classify the items found in them. This was corroborated by Pelfrey and Peacock (1991) that found that there is no uniform concept in their creation and that they vary widely in content.

Second, codes of ethics do not look alike. For Pelfrey and Peacock (1991), codes of ethics vary widely as far as style is concerned, though as White and Montgomery (1980), Benson (1989), and Robin et al (1989) all seem to notice, there is a penchant to being legalistic.

Third, companies do not use the same approach or tone in presenting the contents of their code of ethics. Researchers have found variances in the specific alignment that companies take towards ethical content. For example, Frankel (1989) distinguishes that there are three types of codes according to subject matter: a) codes that contain statements of ideals to which one should strive are called inspirational; b) codes that set down rules that govern conduct which are used to adjudicate grievances are called regulatory; c) codes that reinforce understanding of the prescriptive features with extensive commentary and interpretation are called educational. To these three categories, Vinten (1990) adds a fourth which he calls «aspirational» in that they provide a standard to be aspired to. On the other hand, Farrell and Cobbin (1996), for their part, only distinguish two categories of code content. They can be inspirational if the contents are organized with the idea that ethics are about empowering the individual to be ethical. Or they can be prescriptive if the contents describe the behavioural outcomes required as responses to described circumstances or moral hazards.

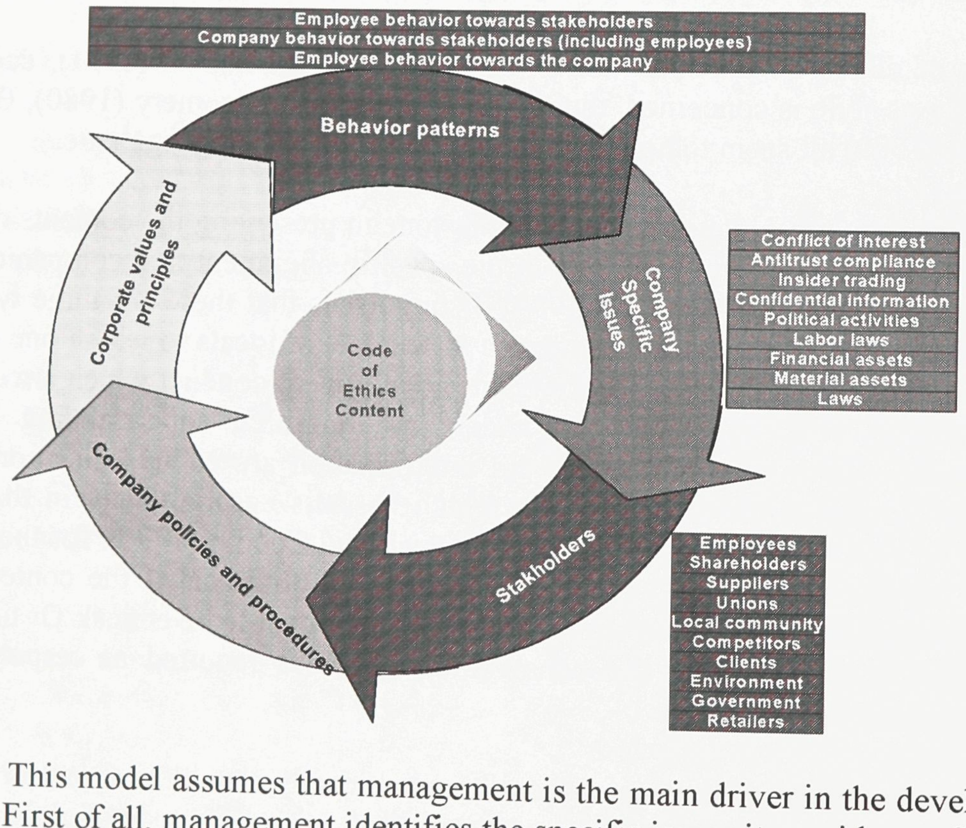
Fourth, there is no general consensus concerning what ideally should be found in a code of ethics. Pelfrey and Peacock (1991) found that companies that prepared a code of ethics did so accordingly to one of three schools of thought on this subject. One says that a code of ethics should address every possible ethical situation. The second says that codes should be simple statements of values. The third says that codes should contain no more than general rules on topics of concern. For their part, Laczniak and Murphy (1985) say that codes of ethics should deal with issues that are specific and pertinent to the industry. Specific problem areas should be uncovered and treated in the code. Finally, for Boudreaux and Steiner (2005), codes should be positive, brief, make reference to relevant policies and documents, and be «aspirational» in tone.

If we put all these considerations together, we distinguish two general characteristics: a) the contents of a code of ethics vary from one company to the next and deal mostly with issues that are company specific; b) the tone and approach used in the document also varies widely from company to company, though they tend to be somewhat legalistic in style. When we combine these two characteristics to the definition that we provided earlier we conclude that code of ethics contain the principles, norms, and standards that employees and the company base their treatment of various company specific issues.

Conceptual Model

Our proposed conceptual model presents the various elements that we have identified that might come into play in a specific code. It considers that there are five elements that make up a code of ethics: a) company specific issues; b) corporate values and principles; c) company policy and procedure; d) various stakeholders; e) behaviour patterns that the company would like to be followed.

Figure 1: proposed conceptual model



This model assumes that management is the main driver in the development of a code of ethics. First of all, management identifies the specific issues it considers sufficiently important to be discussed in a code. One could take as an example the issue of dealing with a supplier. This specific issue might be included in a code of ethics because that the company has in the past had problems of this nature and deems it necessary to talk about it. Then again, maybe the problem has never arisen but that management considers necessary to mention it for preventive reasons. Or still, management has seen this issue developed by other companies and considers that it should follow the lead. Maybe it's an issue that government regulations have made necessary to be addressed by the company. In all, we see that the reasons for developing a particular topic in a code of ethics may be numerous. But because a code of ethics is a working management tool, and not an encyclopaedia of problem areas, the topics that are included in the code are those deemed important by the management of the specific company.

Secondly, once management has identified an issue, it is treated in accordance with the four other factors - elements. For example, maybe the company wants its employees to deal with suppliers in such a fashion that is in accordance with certain values and principles, such as honesty, fair play, integrity and others. The way a problem dealing with suppliers is treated will be in accordance with company policy and procedures. And the way it is worded into the text will take into account the various company stakeholders and the behaviours that the company wants respected.

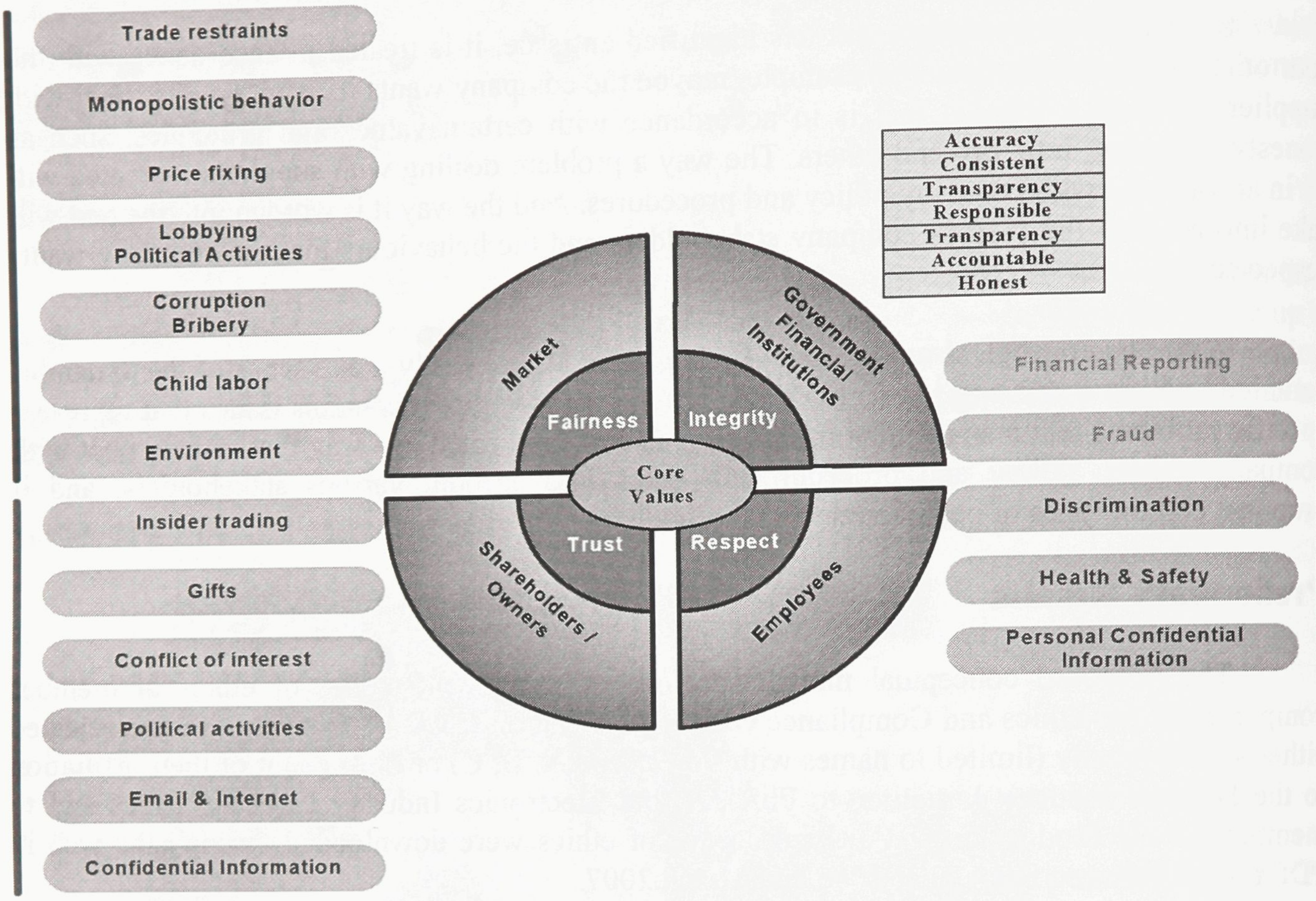
With this conceptual model, a researcher should more easily make sense of the dynamics contained within a particular code of ethics. He/she will see that it contains issues that represent specific problems that management has prioritized and has treated in a way that is congruent with company values, policy and procedures, it takes into account various stakeholders, and it proposes certain types of behaviours.

Preliminary Results

The proposed conceptual model was used to analyse 40 codes of ethics of member companies of the Ethics and Compliance Officer Association (ECOA). Companies were selected either alphabetically (limited to names with first letters A, B, C) or on account of their affiliation to the Defense Industry Initiative, to PhRMA, the Electronics Industry Code of Ethics and to members of the food industry. Analyzed codes of ethics were downloaded through the web in PDF format between September 2006 and March 2007.

Analysis of documents was done by coding content according to the 5 factors included in the conceptual model. However, very soon in the process observations were made that ensued a number of questions. The first observation was that not all member companies of ECOA posted their codes of ethics on their web sites. This surprised and prompted us to ask the question why. Though we cannot provide a definitive answer, we did notice that these companies had one point in common: they were not listed on the New York Stock Exchange (NYSE) or the NASDAQ. Companies listed on these stock exchanges must comply with the 2004 requirement of posting their code of ethics on the web. And so, the codes of ethics that we accessed were mostly of companies listed on the NYSE. A second observation was the prevalence of references to various laws. It appeared as if each ethical value mentioned in the codes was linked to a specific law or a specific rule. This observation changed the way we analysed the codes of ethics. We tried to find whether we could link ethical values mentioned in the documents to a law or a rule. It turned out that we could for most ethical values identified in the documents. Additionally, by grouping the various laws and rules in question, we were able to identify the main stakeholder having an interest in upholding specific values. In the figure number two, we identified four core values and four stakeholders. In the case of the ethical value of respect, we found that it was linked to the laws overseen by the Equal Employment Opportunity Commission, the main stakeholder being employees. It was also linked to laws concerning Health and Safety as well as those protecting an employee's personal confidential information. In the case of the ethical value of trust, we found

Figure 2: Results



that the various rules and regulations concerning issues of insider trading, giving and receiving gifts, conflicts of interest, political activities, the personal use of email and confidential information all go into fostering a relationship of trust between shareholders / owners of a company and its managers and employees. The same is true of the ethical value of integrity. The government and financial institutions are the main stakeholders that require that financial reporting is honest, accurate, and transparent. Finally, the ethical value of fairness is related to a need to keep the market on a level playing field for all players and that no one obtains undue advantage that would destabilize the balance.

In all, our analysis led us to identify four core values (respect, integrity, fairness, trust) and four main stakeholders (employees, government and financial institutions, the market, and shareholders / owners) that seem to be common to the codes of ethics analyzed. The observation of this commonality begged the question of how to explain it. Again, though not a definitive answer, we turn again to the NYSE 2004 rules that require that listed companies include in their code a number of topics: conflict of interest, corporate opportunities, confidentiality, fair dealing, compliance with laws, rules and regulations, reporting of illegal or unethical behavior, protection and proper use of company assets. It now appears that listed companies have adapted their codes to comply with regulatory requirements. Figure 2 reflects the results of these observations.

Discussion

Overall we find that our initial conceptual model (figure 1) remains sound because we did find that codes of ethics possess the five elements that it had identified. However, the initial model assumes that management builds a code of ethics from scratch and determines which issues are to be treated. But as shown in figure 2, the NYSE (2004) requirements change the dynamics, and we see that they determine the main issues and contents of today's code of ethics. A pre-established main structure seems to exist, the NYSE requirements become a minimum, to which management adds-on issues that it finds important. And on account that there seems to be a main structure to codes of ethics, we find figure 2 a better tool in analyzing codes of ethics of companies, at least of those that are listed on the NYSE. This observation brings us to a realization that we further need to validate both models by analyzing the codes of ethics of companies not listed on the NYSE.

Looking at figure 2, we note that only three of the five factors identified in the initial model truly shape the contents of a code of ethics: laws and rules (instead of specific issues), values, and stakeholders. The other two (procedures, policies, and behavior patterns) have lesser roles. This observation echoes what Sanderson and Varner (1984) had found, that codes of ethics contain mostly values that reflect the spirit of a number of laws or regulations of interest to certain stakeholders.

Finally, the fact that core values seem to be shared by many companies makes us wonder whether they correspond to what Donaldson and Dunfee (1994) considered as hypernorms. At the very least, they offer us a composite picture of what an ethical employee looks like: he/ she is a person that is respectful of others, is fair in his/her dealings with market players, demonstrates integrity in providing financial information and is trustful and worthy of company shareholders / owners confidence.

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